PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITOR'S REPORT

Years Ended December 31, 2020 and 2019

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

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December 31, 2020

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Palau National Communications Corporation:

We have audited the accompanying financial statements of the Palau National Communications Corporation (PNCC), a component unit of the Republic of Palau, which comprise the statements of net position as of December 31, 2020 and 2019, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the PNCC's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the PNCC as of December 31, 2020 and 2019, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in Note 11 to the financial statements, the Corporation's operations have been affected by the recent and ongoing outbreak of the coronavirus disease. As a result of the spread of the COVID-19 coronavirus, governments worldwide implemented actions to restrict travel and economic activities. The ultimate disruption which may be caused by the outbreak is uncertain, therefore, the actual impact on the Corporation's business, results of operations, and financial position for the year 2021 and beyond is currently not determinable. Our conclusion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis (MD&A) on pages 4 through 9, the Schedule of Budgetary Comparison information on page 49, Schedule of Proportionate Share of the Net Pension Liability on page 52, and the Schedule of Pension Contributions on page 53, as listed on the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Financial Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Palau National Communications Corporation's basic financial statements. The Schedules of Functional Expenses on page 50 and 51 are presented for the purposes of additional analysis and are not a required part of the basic financial statements. These schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated July 30, 2021, on our consideration of the PNCC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the PNCC's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the PNCC's internal control over financial reporting and compliance.

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BURGER COMER MAGLIARI

Koror, Republic of Palau
July 30, 2021

This section of Palau National Communications Corporation's (PNCC) annual financial report presents the analysis of its financial performance during the year ended December 31, 2020, with comparisons to prior years ended December 31, 2019, and 2018. We encourage readers to consider the information presented here in conjunction with the financial statements and related notes which follows this section.

BUSINESS OVERVIEW

OUR SERVICES

Palau National Communications Corporation was established by RPPL1-40 in 1982 to modernize and expand telecommunications services throughout the Republic of Palau. As a full-service telecommunications provider, PNCC offers nationwide coverage which include Local and Long-Distance Telephone, GSM Mobile, Internet, and Digital TV. Based on the Five (5) Year Growth Trend, Internet subscriptions show average of 26% consistent increase with more customers using HomeNet and prepaid Internet access to Wi-Fi Hotspots. PalauCel (GSM Mobile) had a 24% increase from year 2018 – 2019 but dropped 20% in year 2020 due to the negative impact of COVID-19 on the economy. Both Fixed Line (Telephone) and Digital TV suffered an average decrease of 4% and 13%, respectively, since 2018 due to accelerated usage of mobile telephone service and HomeNet. The trend shows that Internet revenues continues to increase while GSM Mobile, Fixed Line (Telephone), and Digital TV are experiencing a drop in revenue generated.

Five (5) Year Growth Trend
2016 - 2020

Year End December 31	2016	2017	2018	2019	2020
GSM Mobile	**25,770**	**26,546**	**26,524**	**32,868**	**26,359**
Postpaid	2,523	2,916	3,123	3,914	4,742
Prepaid	23,247	23,630	23,401	28,954	21,617
Fixed Line (Telephone)	**7,048**	**7,088**	**7,166**	**6,801**	**6,179**
Business/Government	3,110	3,071	3,047	2,897	2,214
Residential	3,938	4,017	4,119	3,904	3,965
Internet	**2,348**	**3,001**	**3,619**	**3,901**	**4,211**
PalauNet	759	1,008	1,302	1,086	944
DSL	293	328	309	364	390
Domestic Leased Line/VLAN	63	67	62	31	26
Wi-Fi Hotspots	157	195	214	237	242
HomeNet	1,076	1,403	1,732	2,183	2,604
Digital TV	**4,129**	**4,138**	**3,786**	**3,370**	**2,743**
Single Dwelling	3,240	3,260	2,939	2,623	2,377
Multi Units	889	878	847	747	366

FINANCIAL HIGHLIGHTS

At the end of the year 2020, total assets were decreased by $974,421 from the previous year especially with receivables and capital assets with a 33% and 5% reduction, respectively. However, despite the negative impact of COVID-19 pandemic on the economy, PNCC's Investment with Raymond James and Bank of Guam Fidelity Investment had an increase of $489,374, a 22% increase from year 2019.

With the implementation of GASB 67/68 in 2014, Net Pension liabilities kicked in forwarding a negative net position of $9.1 million in 2015. The net income of $3,988,844 realized in 2016 did reduce total negative position down to $5.1 million at the end of 2016, $4,142,899 net income in 2017 reduced the negative position to $.9 million at the end of 2017. The 2018 net income of $2,007,412 fully covered the negative position of $.9 million from 2017 making it a positive $1,034,658 for the year 2018. However, the 2019 negative net income of $1,184,029 reduced the $1,034,658 from 2018 and ending the year 2019 with negative $149,371 net position. With year 2020 negative net income of $1,519,454, the net position for the year further dropped to a net deficiency of $1,668,825.

STATEMENTS OF NET POSITION

Years ended December 31, 2020, 2019, and 2018

	2020	2019	2018
ASSETS			
Current Assets			
Cash	$ 465,082	$ 296,738	$ 787,197
Restricted cash and cash equivalents	250,146	250,113	3,818,176
Receivables, net	1,336,291	1,988,686	2,118,155
Inventories	523,710	519,658	432,493
Prepaid expenses	302,368	217,705	46,214
Total current assets	**$ 2,877,597**	**$ 3,272,900**	**$ 7,202,235**
Investments	2,712,124	2,222,750	1,033,439
Other noncurrent assets	54,300	60,773	54,300
Plant and equipment, net	21,205,813	22,267,832	21,895,505
Total Assets	**$ 26,849,834**	**$ 27,824,255**	**$ 30,185,479**
Deferred outflows of resources:			
Deferred outflows from pension	4,284,465	2,000,476	2,007,702
Total Assets	**$ 31,134,299**	**$ 29,824,731**	**$ 32,193,181**
LIABILITIES AND NET POSITION			
Current liabilities			
Current portion of long-term debt	$ 2,357,943	$ 1,531,736	$ 1,463,147
Accounts payable	1,610,170	1,028,617	1,109,509
Payable to carriers, net	13,566	-	17,357
Accrued expenses	401,735	465,262	348,609
Unearned revenues	-	900	220
Customer deposits	570,197	621,054	669,363
Total current liabilities	**$ 4,953,611**	**$ 3,647,569**	**$ 3,608,205**
Note payable, net of current portion	14,235,792	15,839,333	17,373,552
Net Pension Liability	11,837,827	8,712,379	8,539,634
Total liabilities	**$ 31,027,230**	**$ 28,199,281**	**$ 29,521,391**
Defered inflows of resources			
Deferred inflows from Pension	$ 1,775,894	$ 1,774,821	$ 1,637,132
Commitment and contigencies			
Net position:			
Invested capital assets, net of related debt	4,612,078	4,896,763	3,058,806
Restricted - Debt service reserve	250,146	250,113	3,818,176
Unrestricted	(6,531,049)	(5,296,247)	(5,842,324)
Total net position	**$ (1,668,825)**	**$ (149,371)**	**$ 1,034,658**
Total Liabilities and Net Position	**$ 31,134,299**	**$ 29,824,731**	**$ 32,193,181**

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

Years ended December 31, 2020, 2019, and 2018

	2020	2019	2018
Operating revenues			
Long Distance	$ (16,391)	$ 186,416	$ 237,184
Local	1,700,249	1,507,815	1,526,232
PalauNet	3,129,431	3,094,399	3,972,763
Digital TV	1,227,625	1,448,376	1,668,337
GSM Mobile	6,189,716	7,371,235	8,545,157
Miscellaneous	142,446	247,797	146,419
Provision for doubtful accounts	(104,816)	(121,536)	(142,214)
Total Operating Revenues	**$ 12,268,260**	**$ 13,734,502**	**$ 15,953,878**
Operating expenses			
Depreciation	2,804,804	2,669,183	2,217,905
Plant specific operations	5,500,240	6,290,280	6,534,939
Corporate operations	2,754,262	2,853,615	1,886,911
Customer service operations	1,629,054	1,674,426	1,520,148
Plant non-specific operations	854,868	610,465	744,017
Total Operating Expenses	**$ 13,543,228**	**$ 14,097,969**	**$ 12,903,920**
Earnings from operations	**$ (1,274,968)**	**$ (363,467)**	**$ 3,049,958**
Nonoperating income (expenses):			
Unrealized gain (loss) on investments	527,520	59,488	(128,981)
Realized gain on investments	-	49,370	30,561
Interest (expense)	(770,106)	(840,515)	(914,311)
Gain/(Loss) on investments	-	9,899	25,903
Other income (expense)	(1,900)	(98,804)	(55,718)
Total nonoperating income (expenses), net	**$ (244,486)**	**$ (820,562)**	**$ (1,042,546)**
Change in net position	**$ (1,519,454)**	**$ (1,184,029)**	**$ 2,007,412**
Net position at beginning of year	$ (149,371.00)	$ 1,034,658	$ (972,754)
Net position at end of year	**$ (1,668,825)**	**$ (149,371)**	**$ 1,034,658**

Total operating revenues had decrease of 11% from $13.7 million in 2019 to $12.2 million in 2020. The decrease in total revenues is attributable to the decline in Long Distance, GSM Mobile, and Digital TV.

Total operating expenses decreased 4% or $554,741 in 2020 as result of efficient cost reduction in Plant Specific Operations, Corporate Operations, and Customer Service Operations.

Operating loss from operations increased by $911,501 or 251% from negative $363,467 in 2019 to negative $1,274,968 in 2020. In compliance with GASB 67&68, $8.7 million in 2019 and $11.8 million in 2020 liabilities resulted in cumulative deficit of $1,668,825 at end of 2020 as the net position for the year.

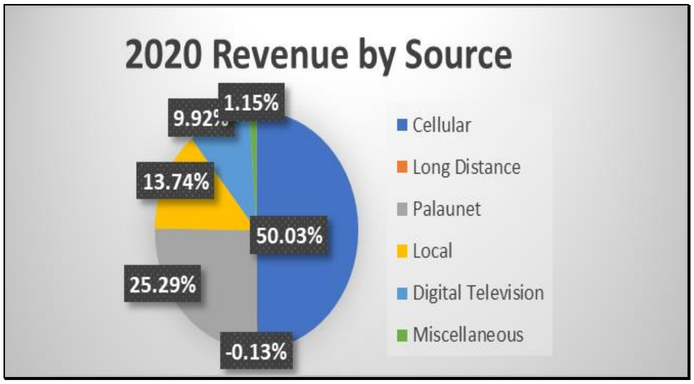
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

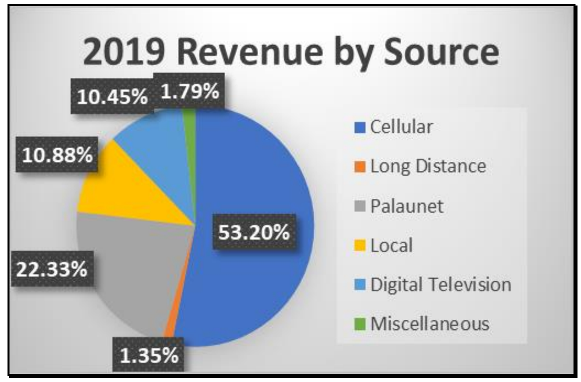
	2020	2019	Increas/(Decrease) Dollar	Percent	2018
Operating revenues	$ 12,268,260	$ 13,734,502	$ (1,466,242)	-9.19%	$ 15,953,878
Operating expenses	$ (13,543,228)	$ (14,097,969)	$ 554,741	-4.30%	$ (12,903,920)
Operating income	$ (1,274,968)	$ (363,467)	$ (911,501)	-29.89%	$ 3,049,958
Non-operating income (expenses)	$ (244,486)	$ (820,562)	$ 576,076	-55.26%	$ (1,042,546)
Change in net position	**$ (1,519,454)**	**$ (1,184,029)**	**$ (335,425)**	**-16.71%**	**$ 2,007,412**

REVENUE BY SOURCE

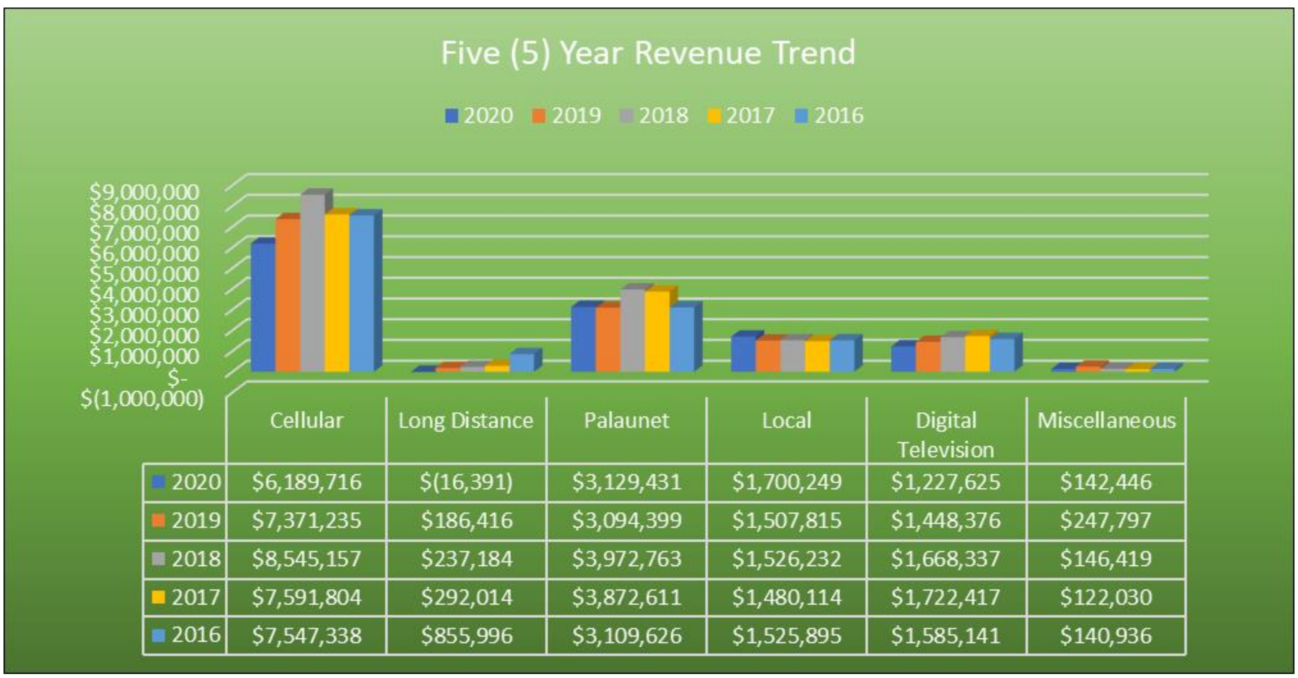
Revenue Source	2020	2019	Increase/(Decrease Dollar	Percent	2018
Cellular	$ 6,189,716	$ 7,371,235	$ (1,181,519)	-16.03%	$ 8,545,157
Long Distance	(16,391)	186,416	$ (202,807)	-108.79%	237,184
Palaunet	3,129,431	3,094,399	$ 35,032	1.13%	3,972,763
Local	1,700,249	1,507,815	$ 192,434	12.76%	1,526,232
Digital Television	1,227,625	1,448,376	$ (220,751)	-15.24%	1,668,337
Miscellaneous	142,446	247,797	$ (105,351)	-42.52%	146,419
Provision for doubtful accts	(104,816)	(121,536)	$ 16,720	-13.76%	(142,214)
Total	**$ 12,268,260**	**$ 13,734,502**	$ (1,466,242)	-10.68%	**$ 15,953,878**

Cellular operations which contributed the highest source of revenue over the previous years went down by 16% in year 2020, including Long Distance (108%) and Digital TV (15%). With the closure of country's borders due to COVID-19 pandemic caused slump in tourism industry which affected revenue generation especially in Long Distance and GSM Mobile operations. In addition, the decrease in Long Distance and Digital Television revenue is due to the reliance on Internet for entertainment and communication.





Summarized in the chart above are the major revenue sources. For 2020, the cellular operations contributed about 50% of the total operating revenues. The chart below shows the change in revenues by source over the past five years.



	Cellular	Long Distance	Palaunet	Local	Digital Television	Miscellaneous
2020	$6,189,716	$(16,391)	$3,129,431	$1,700,249	$1,227,625	$142,446
2019	$7,371,235	$186,416	$3,094,399	$1,507,815	$1,448,376	$247,797
2018	$8,545,157	$237,184	$3,972,763	$1,526,232	$1,668,337	$146,419
2017	$7,591,804	$292,014	$3,872,611	$1,480,114	$1,722,417	$122,030
2016	$7,547,338	$855,996	$3,109,626	$1,525,895	$1,585,141	$140,936

SUMMARY OF FINANCIAL RESULTS AND STRATEGIC PLANNING

Summary of Financial Results for 2020

As shown in Table 1 – *Statement of Revenues, Expenses and Changes in Net Position,* PNCC's 2020 revenue decreased by 9.19% over the previous year. The negative change in net position at the end of 2020 did increase the cumulative deficit from $149,371 in 2019 to $1,668,825.

- Local: The revenue trend shows an increase of 12.76% compared to 2019.
- PalauNet: The revenue trend shows an increase of 1.13% compared to 2019. This is attributed to increase in HomeNet sign-ups and usage of prepaid Internet access to Wi-Fi Hotspots.
- PalauCel: The revenue trend shows a decrease of 16% compared to 2019. The decrease in revenue is attributed to the negative impact of COVID-19 pandemic on the economy.
- Digital TV: The revenue trend shows a decrease of 15.2% compared to 2019. The decrease in revenue is attributed to increase preference on Netflix, Youtube, Facebook, and other media entertainment.

PNCC Strategic Planning Process

The PNCC's 5-year Mid-Term Business Plan (2014-2018), developed with expert assistance of Mr. Akira Maeda in 2013 provides road map for financial sustainability of the corporation. Based on the Business Plan, PNCC implemented 3G platform in 2015 to advance its GSM cellular services. In 2016, PNCC completed the expansion of 3G service coverage to the whole Babeldaod, Peleliu and Angaur. In 2017, PNCC implemented the more advanced 4G services and improve quality of service for customer retention and penetration of the tourism market. PNCC updated its Strategic Plans in 2018 which covers 5 years period (2019 – 2024).

CONTACTING PNCC'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of PNCC's finances and to demonstrate PNCC's transparency, accountability and stewardship for the money it receives. The Management's Discussion and Analysis for the year ended December 31, 2020, is set forth in the report on the audit of PNCC. The discussion and analysis explained the major factors impacting the 2020 financial statements. If you have questions or need additional information, please contact the Chief Financial Officer at the Palau National Communications Corporation, P.O. Box 99, Koror, Republic of Palau 96940, or e-mail rramarui@pnccpalau.com or call 587-9000.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

FINANCIAL SECTION

Years Ended December 31, 2020 and 2019

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Statements of Net Position
December 31, 2020 and 2019

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

	2020	2019
Current assets:		
Cash (Notes 2, 3, 6 and 9)	$ 465,082	$ 296,738
Receivables: (Notes 2, 5 and 9)		
Trade	1,838,816	1,822,812
Related party (Note 5)	391,212	729,230
Carriers, net	348,882	557,422
Other receivable	(402)	15,173
Allowance for doubtful accounts (Note 2)	(1,242,217)	(1,135,951)
Total receivables, net	1,336,291	1,988,686
Inventories, net (Note 2)	523,710	519,658
Prepaid expenses (Note 7)	302,368	217,705
Total current assets	2,627,451	3,022,787
Investments (Notes 2, 3 and 9)	2,712,124	2,222,750
Restricted cash and cash equivalents (Notes 2, 3, 6 and 9)	250,146	250,113
Other noncurrent assets (Note 2)	54,300	60,773
Capital assets, net (Notes 2, 4, 6)	21,205,813	22,267,832
Total assets	26,849,834	27,824,255
Deferred outflows of resources:		
Deferred outflows from pension (Note 2)	4,284,465	2,000,476
Total assets and deferred outflows of resources	$ 31,134,299	$ 29,824,731

LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION

	2020	2019
Current liabilities:		
Current portion of long-term debt (Notes 6 and 9)	$ 2,357,943	$ 1,531,736
Accounts payable (Note 9)	1,610,170	1,028,617
Payable to carriers, net (Note 9)	13,566	-
Accrued expenses (Notes 2 and 9)	401,735	465,262
Unearned revenues (Notes 2 and 9)	-	900
Customer deposits (Notes 2 and 9)	570,197	621,054
Total current liabilities	4,953,611	3,647,569
Note payable, net of current portion (Notes 6 and 9)	14,235,792	15,839,333
Net pension liability (Notes 2 and 6)	11,837,827	8,712,379
Total liabilities	31,027,230	28,199,281
Deferred inflows of resources:		
Deferred inflows from pension (Note 2)	1,775,894	1,774,821
Commitments and contingencies (Note 7)		
Net position (Note 2):		
Net investment in capital assets	4,612,078	4,896,763
Restricted for:		
Debt service and reserve	250,146	250,113
Unrestricted	(6,531,049)	(5,296,247)
Total net position	(1,668,825)	(149,371)
Total liabilities, deferred inflows of resources and net position	$ 31,134,299	$ 29,824,731

See accompanying notes to financial statements.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Statements of Revenues, Expenses and Changes in Net Position
For The Years Ended December 31, 2020 and 2019

	2020	2019
Operating revenues (Note 2):		
Cellular	$ 6,189,716	$ 7,371,235
Palaunet	3,129,431	3,094,399
Local	1,700,249	1,507,815
Digital television	1,227,625	1,448,376
Long distance	(16,391)	186,416
Miscellaneous	142,446	247,797
Provision for doubtful accounts	(104,816)	(121,536)
Total net operating revenues	12,268,260	13,734,502
Operating expenses:		
Plant specific:		
Operations	5,500,240	6,290,280
Depreciation (Note 4)	2,804,804	2,669,183
Corporate office	2,754,262	2,853,615
Customer service	1,629,054	1,674,426
Plant non-specific operations	854,868	610,465
Total operating expenses	13,543,228	14,097,969
Operating income loss	(1,274,968)	(363,467)
Nonoperating income (expense):		
Unrealized gain (loss) on investments	527,520	59,488
Realized gain on investments	-	49,370
Income on investments	-	9,899
Other income (expense), net	(1,900)	(98,804)
Interest expense (Note 6)	(770,106)	(840,515)
Total nonoperating income (expense), net	(244,486)	(820,562)
Change in net position	(1,519,454)	(1,184,029)
Net position (deficit) at beginning of year (Note 2)	(149,371)	1,034,658
Net position (deficit) at end of year	$ (1,668,825)	$ (149,371)

See accompanying notes to financial statements.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Statements of Cash Flows
For the Years Ended December 31, 2020 and 2019

	2020	2019
Cash flows from operating activities:		
Cash received from customers	$ 12,399,677	$ 13,516,894
Cash payments to suppliers for goods and services	(8,110,812)	(8,108,115)
Cash payments to employees	(1,361,570)	(3,001,890)
Net cash provided by operating activities	2,927,295	2,406,889
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(1,742,784)	(3,041,509)
Additions from restricted cash and cash equivalents	(33)	-
Transfers from restricted cash and cash equivalents	-	3,568,063
Interest paid	(770,106)	(840,515)
Repayment of long-term debt	(777,334)	(1,465,630)
Net cash used in financing activities	(3,290,257)	(1,779,591)
Cash flows from investing activities:		
Other income	(1,900)	(98,804)
Unrealized gain (loss) on investments	527,519	-
Proceeds from sale and maturities of investment securities	798,924	301,586
Proceeds from sale of assets	-	-
Purchase of investment securities	(793,237)	(1,320,539)
Net cash used in investing activities	531,306	(1,117,757)
Net change in cash	168,344	(490,459)
Cash at beginning of year	296,738	787,197
Cash at end of year	$ 465,082	$ 296,738

See accompanying notes to financial statements.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Statements of Cash Flows, Continued
For the Years Ended December 31, 2020 and 2019

	2020	2019
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	$ (1,274,968)	$ (363,467)
Adjustments to reconcile operating income to net cash provided by (used for) operating activities:		
Depreciation	2,804,804	2,669,183
Pension cost	842,532	317,660
Unrealized gain on investments	(527,520)	(59,488)
Provision for doubtful accounts	104,816	121,536
Other income (expense), net	1,900	98,804
Realized gain on investments	-	(49,370)
Income on investments	-	(9,899)
(Increase) decrease in assets:		
Receivables:		
Trade	16,004	153,243
Related party	338,018	(41,766)
Carriers, net	208,540	(163,302)
Other receivable	15,575	28,109
Inventories	(4,052)	(87,165)
Prepaid expenses	(84,663)	(171,491)
Other noncurrent assets	6,473	(6,473)
Increase (decrease) in liabilities:		
Accounts payable	581,553	(80,892)
Payable to carriers, net	13,566	(17,357)
Accrued expenses	(63,526)	116,653
Customer deposits	(50,857)	(48,309)
Unearned revenues	(900)	680
Net cash provided by operating activities	$ 2,927,295	$ 2,406,889

See accompanying notes to financial statements.

(1) Organization

Palau National Communications Corporation (PNCC), a component unit of the Republic of Palau (ROP), was created on August 23, 1982, under the provisions of the Republic of Palau Public Law (RPPL) 1-40. The law created a wholly owned government corporation managed by five (5) members of a Board of Directors appointed by the President of the ROP, with the advice and consent of the Senate of the Olbiil Era Kelulau (ROP National Congress).

The primary purpose of PNCC is to establish and operate communications services as a communication common carrier within the ROP. PNCC conducts its operations on land and in buildings provided by the National Government of the ROP. PNCC has four divisions: PNCC, PNCC Wireless (Wireless), Digital Cable Television (DTV) formerly known as Island Cable Television (ICTV), and Palaunet, which provides local and long distance telephone services, cellular telecommunications services and equipment, digital cable television services, and internet services, respectively, within the ROP.

(2) Summary of Significant Accounting Policies

The accounting policies of PNCC conform to accounting principles generally accepted in the United States of America as applicable to governmental entities, specifically proprietary funds. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

A. Basis of Presentation

The financial statements of PNCC have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental entities. In 2012, PNCC adopted Government Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This Statement identifies and consolidates accounting and financial reporting provisions that apply to state and local governments. Prior to the issuance of Statement No. 62, PNCC applied the standards and principles outlined in GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary and Other Governmental Entities that Use Proprietary Fund Accounting*. GASB Statement No. 62, which supersedes Statement No. 20, is the primary resource for accounting guidance and principles.

(2) Summary of Significant Accounting Policies, continued

A. Basis of Presentation, continued

PNCC implemented GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Government as amended by* GASB Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus,* GASB Statement No. 38, *Certain Financial Statement Note Disclosures, and* GASB Statement No. 63*, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* in the statement of financial position.

PNCC follows the business-type activities requirements of GASB Statement No. 34. This approach requires the following components of PNCC's financial statements:

- Management's discussion and analysis

- Basic financial statements, including a statement of net position, statement of revenues, expenses and changes in net position and a statement of cash flows using the direct method; and

- Notes to financial statements

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* required the PNCC to establish net position categories as follows:

Net investment in capital assets:

Capital assets net of accumulated depreciation, reduced by the outstanding principal balances of debt attributable to the acquisition, construction or improvements of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt should be included in this component of net position. At December 31, 2020 and 2019, PNCC has deferred outflows of resources and deferred inflows of resources that are included as a component of net position.

Restricted:

Restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported. At December 31, 2020 and 2019, PNCC have deferred outflows of resources and deferred inflows of resources that was included as a component of restricted net position.

(2) Summary of Significant Accounting Policies, continued

A. Basis of Presentation, ccontinued

PNCC's component of net position, continued

Restricted net position, continued

The PNCC's restricted net position categories are as follows:

Nonexpendable: Net position subject to externally imposed stipulations that require PNCC to maintain them permanently. At December 31, 2020 and 2019, PNCC did not have any nonexpendable net position.

Expendable: Net position whose use by PNCC is subject to externally imposed stipulations that can be fulfilled by actions of the PNCC pursuant to those stipulations or release of those stipulations by the passage of time.

Assets that have been assigned as collateral for the Rural Utilities Service (RUS) loan are classified as restricted.

Unrestricted:

Net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted components of net position. Unrestricted net position may be designated for specific purposes by action of the Board of Directors or may otherwise be limited by contractual agreements with outside parties. At December 31, 2020 and 2019, PNCC had deferred outflows of resources and deferred inflows of resources that are included as a component of net position.

B. Measurement Focus and Basis of Accounting

Measurement focus refers to timing of recognition, that is, when revenues and expenditures, expenses, and transfers and assets, deferred outflows of resources, liabilities and deferred inflows of resources are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

The accrual basis of accounting is utilized by proprietary funds. Under the accrual method, revenues are recorded when earned and expenses recorded at the time liabilities are incurred. PNCC uses the accrual basis of accounting.

(2) Summary of Significant Accounting Policies, continued

B. Measurement Focus and Basis of Accounting, continued

PNCC maintains a chart of accounts in accordance with the Uniform System of Accounts for telephone companies of the United States of America Federal Communication Commission's Rules, and in conformity with accounting principles generally accepted in the United States of America (GAAP).

C. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for uncollectible accounts receivable and management's estimate of depreciation expense which is based on estimated useful lives of the respective assets. The allowance for uncollectible accounts receivable is determined based on management estimates. While management believes the amount is adequate, the ultimate uncollectible balance may differ from the amounts provided.

D. Budget

In accordance with the ROP Code, the Board of Directors of PNCC adopts an annual budget on a proprietary fund basis and the budget is used as a management tool throughout the accounting cycle. All operating and capital expenditures and revenues are identified in the budgeting process. PNCC's budget is presented to the Olbiil Era Kelulau (OEK) for its review and comments no later than sixty days (60 days) before the budget's effective date (November 1). Pursuant to regulation of the ROP, after PNCC has repaid the RUS loan, PNCC is required to submit a detailed and itemized budget to the OEK for its approval no later than 60 days before it is to take effect.

Throughout the year, PNCC monitors and evaluates expenditure levels and patterns. The Board of Directors may authorize revisions to the budget based on the availability of financial resources. Formal budget revisions are authorized in the same manner as original budget submissions.

(2) Summary of Significant Accounting Policies, continued

D. Budget, continued

The supplementary information in the Management's Discussion and Analysis in pages 4 to 9 includes PNCC's analysis of the significant variations and major factors impacting the 2019 and prior years within its five-year strategic plan and the currently known reasons for those significant variations that PNCC expects to affect its liquidity or ability to provide future services.

E. New Accounting Standards

During the year ended December 31, 2020, GASB issued Statement No. 95, *Postponement of the Effective Dates of Certain Authoritative Guidance*, which postpones the effective dates of GASB Statement Nos. 84, 89, 90, 91, 92 and 93 by one year and GASB Statement No. 87 by 18 months; however, earlier application of the provisions addressed in GASB Statement No. 95 is encouraged and is permitted to the extent specified in ach pronouncement as originally issues. In accordance with GASB Statement No. 95, management elected to postpone implementation of these Statements.

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities.* This Statement improves guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The requirements of this Statement will enhance consistency and comparability by (1) establishing specific criteria for identifying activities that should be reported as fiduciary activities and (2) clarifying whether and how business-type activities should report fiduciary activities. Pursuant to GASB Statement No. 95, GASB Statement No. 84 will be effective for December 31, 2021. Management does not believe that the implementation of this Statement will have a material effect on PNCC's financial statements.

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and as inflows of resources or outflows of resources recognized based on the payment provisions of the contract. GASB Statement No. 87 will be effective for PNCC for the fiscal year ending December 15, 2019. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

(2) Summary of Significant Accounting Policies, continued

E. New Accounting Standards, continued

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred Before the End of a Construction Period*. The objectives of this Statement are (1) to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and (2) to simplify accounting for interest cost incurred before the end of a construction period. Pursuant to GASB Statement No. 95, GASB Statement No. 89 will be effective for the year ended December 31, 2022. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

In March 2018, GASB issued Statement No. 90, *Majority Equity Interests – An Amendment of GASB Statements No. 14 and 61*. The primary objectives of this Statement are to improve the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. It defines a majority equity interest and specifies that a majority equity interest in a legally separate organization should be reported as an investment if a government's holding of the equity interest meets the definition of an investment. A majority equity interest that meets the definition of an investment should be measured using the equity method, unless it is held by a special-purpose government engaged only in fiduciary activities, a fiduciary fund, or an endowment (including permanent and term endowments) or permanent fund. Pursuant to GASB Statement No. 95, GASB Statement No. 90 will be effective for the year ended December 31, 2021. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

In May 2019, GASB issued Statement No. 91 *Conduit Debt Obligations*. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures. Pursuant to GASB Statement No. 95, GASB Statement No. 91 will be effective for the year ended December 31, 2023. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

(2) Summary of Significant Accounting Policies, continued

E. New Accounting Standards, continued

In January 2020, GASB issued Statement No. 92, *Omnibus 2020*. The requirements of this Statement will enhance comparability in the application of accounting and financial reporting requirements and will improve the consistency of authoritative literature addressing practice issues that have been identified during the implementation and application of certain GASB Statements. This Statement addresses a variety of topics and includes specific provisions about effective date of Statement No. 87, *Leases*; for interim financial statements, the terminology used to refer to derivative instruments and the applicability of certain requirements of Statement No. 84, Fiduciary Activities, to postemployment. The requirements related to the effective date of GASB Statement No. 87 and Implementation Guide 2019-3, reissuance recoveries and terminology used to refer to derivative instruments are effective upon issuance. The remaining requirements of GASB Statement No. 92 are for year ending December 31, 2022. Management does not believe that the implementation of this Statement and Guide 2019-3 will have a material effect on the PNCC's financial statements.

In April 2020, GASB is issued Statement No. 93, *Replacement of Interbank Offered Rates* (IBOR). The primary objective of this Statement is to address those and other accounting and financial reporting implications of the replacement of IBOR. Pursuant to GASB Statement No. 95, GASB Statement No. 93 will be effective for the year ended December 31, 2022. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

In March 2020, GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The primary objective of this Statement is to improve financial reporting by addressing issue related to public-private and public-public partnership arrangements. This Statement also improves guidance for accounting and financial reporting for availability payment arrangements. GASB Statement No. 94 will be effective for the year ending December 31, 2023. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

In May 2020, GASB issued Statement No. 96, Subscription-Based Information Technology Arrangements. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users. This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-of-use subscription asset – an intangible asset and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBIT; and (4) requires note disclosures regarding a SBITA. GASB Statement No. 96 will be effective for the year ended December 31, 2023. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

(2) Summary of Significant Accounting Policies, continued

E. New Accounting Standards, continued

In June 2020, GASB issued Statement No. 97, *Certain Component Unit Criteria and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans – amendment of GASB Statement Nos. 14 and 84, and a supersession of GASB Statement No. 32*. The primary objectives of this Statement are to (1) increase consistency and comparability related to the reporting of fiduciary component units in circumstances in which a potential component unit does have a governing board and the primary government performs the duties that a governing board typically would perform; (2) mitigate costs associated with the reporting of certain defined contribution pension plans, defined contribution other postemployment benefit (OPEB) plans as fiduciary component units in fiduciary fund financial statements; and (3) enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans. GASB Statement No. 97 will be effective for the year ended December 31, 2022. Management does not believe that the implementation of this Statement will have a material effect on the PNCC's financial statements.

F. Assets, Liabilities and Net Position

Cash

Cash in the statement of cash flows includes cash on hand and cash in checking and savings accounts.

Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents, including amounts restricted for repayment of debt owed to Rural Utilities Service (RUS), amounts restricted for contracts approved by the RUS and RUS revenues, are separately classified in the Statements of Net Position.

Receivables and Allowance for Doubtful Accounts

PNCC grants credit on an unsecured basis to individuals, businesses and governmental entities that are situated in the Republic of Palau, the United States of America, Japan and the Territory of Guam.

The allowance for doubtful accounts is stated at an amount which management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. The allowance is established through a provision for uncollectible receivables charged to expense.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Allowance for Doubtful Accounts

An analysis of the change in allowance for doubtful accounts for the years ended December 31, 2020 and 2019 is as follows:

	2020	2019
Balance at beginning of the year	$ 1,135,951	$ 1,014,415
Current year provision	106,266	121,536
Balance at end of year	$ 1,242,217	$ 1,135,951

Inventories

Inventories comprise telecommunication equipment, parts and cables and are stated at the lower of cost (average cost method) or market.

Investments

Credit risk for investments is the risk that an issuer or other counterparty to an investment will not fulfill its obligations.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in any one issuer that represents five percent (5%) or more of total investments for the PNCC. At December 31, 2020 and 2019, there were no investments in any one issuer that exceeded five percent (5%) of total investments.

PNCC has formal policies in place as of December 31, 2020 and 2019 to address investment risks. The following investment policy governs the investment of assets of PNCC:

General:

- Any restrictions set forth by applicable law governing limits, size, or quality of investments, if more stringent than those of this investment policy, will be the governing restriction.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Investments, continued

- U.S. and non-U.S. common stocks, ADRs (American Depository Receipts), convertible bonds, preferred stocks, fixed-income securities, mutual funds and short-term securities are permissible investments.

- No individual security of any issuer, other than that of the United States Government, shall constitute more than 10% (at cost) of any Investment Manager's portfolio.

- Holdings of any issuer shall constitute no more than 5% of the outstanding securities of such issuer.

- Investments in a registered mutual fund managed by the Investment Manager are subject to prior approval by the Board of Directors.

- The following securities and transactions are not authorized: letter stock and other unregistered securities; non-negotiable securities; commodities or other commodity contracts; and short sales or margin transactions. Options and futures are restricted, except by petition to the Board of Directors for approval.

Equities:

- Consistent with the desire to maintain broad diversification, allocations to any economic or industry sector should not be excessive. Comparisons to peer group characteristics will be used to evaluate and to assure consistency of each manager's stated strategy and style.

- Equity holdings shall be restricted to readily marketable securities of corporations that are actively traded on the major exchanges and over the counter.

- The Investment Managers shall have the discretion to invest a portion of the assets in cash reserves when they deem appropriate. However, the Investment Managers will be evaluated against their peers on the performance of the total funds under their direct management.

- Common stock and preferred stock of any institution or entity created or existing under the laws of the United States of America or any state, district, territory, or District of Columbia, or of any foreign country are permissible investments.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Investments, continued

U.S. Fixed Income:

- All fixed income securities (with the exception of U.S. Treasury or Agency securities which are unrated) shall have a Moody's, Standard & Poor's and/or a Fitch's credit quality rating of no less than "BBB".

- No more than 20% of the market value of the portfolio shall be rated less than single "A" quality, unless the Investment Manager has specific written authorization. Total portfolio quality (capitalization weighted) shall maintain an "A" minimum rating.

Cash/Cash Equivalents:

- The following investments will be permitted:
  1. U.S. Government obligations, U.S. Government agency obligations, and U.S. Government instrumentality obligations.

  2. Commercial Paper: All commercial paper issuers must maintain an "A-1" rating by Standard & Poor's Corporation and a "P-1" rating by Moody's Investor Service and be issued by corporations having total assets in excess of one billion dollars ($1,000,000,000).

  3. Certificates of Deposit: All certificate of deposit issuers must have a minimum capital of ten million dollars ($10,000,000).

  4. Repurchase Agreements: Repurchase agreements must be collateralized with either: (1) U.S. Treasury or Agency Securities with a market value of 102%, marked to market daily; or (2) money market instruments which meet the qualifications of the Statement and with a market value of 102%, marked to market daily.

  5. Money Market Funds: Money Market Funds must be registered with the Securities and Exchange Commission (SEC) under the Investment Company Act of 1940.

- No single issue shall have a maturity of greater than one (1) year.

- The money market funds must have an average maturity of less than one (1) year.

GASB Statement No. 40 requires entities to provide information about the credit risk associated with their investments by disclosing the credit quality ratings.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Capital Assets

Capital assets are stated at cost less accumulated depreciation and any impairment in value. Depreciation expense is provided using the straight-line method over the estimated useful lives of the respective assets. Major improvements and betterments which increase the usefulness and efficiency or prolong the life of the asset are capitalized, while the costs of maintenance and repairs, including the cost of replacing minor items not constituting substantial betterments, are charged to expense as these costs are incurred.

Depreciation expense for all capital assets is provided for on the straight-line basis over the following estimated useful lives:

	Estimated Useful Lives
Telecommunications equipment	5 - 25 years
Central office equipment	3 - 17 years
Building and general support equipment	3 - 30 years
Cable television equipment	2 - 20 years
Wireless equipment	3 - 15 years
Furniture and fixtures	5 - 10 years
Vehicles	6 years

Review of Carrying Value of Capital Assets for Impairment

PNCC reviews the carrying value of capital assets for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The factors considered by management in performing this assessment include current operating results, trends, and prospects, as well as the effects of obsolescence, demand, competition, and other economic factors. The management of PNCC does not believe that any impairment exists for the years ending December 31, 2020 and 2019.

Capitalization of Interest

Interest is capitalized by PNCC when it is determined to be material. PNCC capitalizes interest in accordance with GASB Statement No. 62. Interest is capitalized for costs incurred on funds used to construct or acquire property, plant and equipment. The capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Other Noncurrent Assets

Other noncurrent assets represent refundable deposits related to PNCC's subscription of television channels and programs for its digital television services. At December 31, 2020 and 2019, refundable deposit was $54,300 and $60,773, respectively, and are reflected as other noncurrent assets in the accompanying financial statements.

Compensated Absences

Compensated absences are those absences for which employees will be paid, such as annual vacation leave and health (sick) leave. PNCC recognizes all vested vacation leave benefits accrued by its employees when earned. Employees are credited annual leave with pay of 80, 120, and 160 hours per year depending upon their length of service with PNCC. An employee cannot carry over to the following calendar year accumulated annual vacation leave in excess of 80 hours for 5 to 9 years of service, and 120 hours for employees with over 10 years of service. However, a carryover of additional annual leave may be allowed upon request and approval by the Management when it is determined to be in the interest of PNCC. At December 31, 2020 and 2019 accrued annual leave totaled $155,748 and $116,516, respectively, and is included in the Statements of Net Position as a component of accrued expenses. At December 31, 2020 and 2019, all compensated absences are current. For the years ended December 31, 2020 and 2019, annual vacation leave taken totaled $121,533 and $135,233, respectively, and is included in the Statements of Revenues, Expenses and Changes in Net Position as a component of operating expenses. No liability is recorded for non-vesting accumulating rights to receive health or sick pay benefits.

Unearned Revenues

Unearned revenues consist of cash payments received from customers for which goods or services have not been earned or realized, and prepaid long distance sales in which actual traffic minutes were used and processed after the reporting period. At December 31, 2020 and 2019, unearned revenues from prepaid telecom billings were $0 and $900, respectively. Management has not determined the unearned revenue from prepaid long-distance sales.

Customer Deposits

Customer deposits consist of subscriber deposits, installation fees and amounts received for related services and subscriptions to be provided in future periods. PNCC's requirement of customer deposit amount varies depending on the type of service or subscription applied for. These deposits are eligible for refunding after twelve (12) consecutive months of prompt payment history. If a deposit is held on an account at the time services are terminated, the deposit will be applied to the unpaid balance and a refund check is issued for the remainder.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Customer Deposits, continued

Refunds are not automatic; the customer must request a refund. There is no interest paid on customer deposits. At December 31, 2020 and 2019, customer deposits totaled $570,197 and $621,054, respectively.

Advertising Costs

Advertising costs are expensed as incurred. For years ended December 31, 2020 and 2019, advertising costs totaled $3,082 and $2,050, respectively, and are included as a component of customer service operations expense reported in the Statements of Revenues, Expenses and Changes in Net Position.

Deferred Outflows of Resources

In addition to assets, the statements of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (deduction of net position) until then. PNCC determined the differences between expected and actual experience with regard to economic or demographic factors in the measurement of the total pension liability, pension contributions made subsequent to the measurement date and changes in proportion and difference between PNCC pension contributions and proportionate share of contributions qualify for reporting in this category.

Deferred Inflows of Resources

In additions to liabilities, the statements of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (additions to net position) until then. PNCC has determined the difference between projected and actual earnings on pension plan investments qualify for reporting in this category.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Pensions

Pensions are required to be recognized and disclosed using the accrual basis of accounting. PNCC recognizes a net pension liability for the defined benefit pension plan in which it participates, which represents PNCC's proportional share of excess total pension liability over the pension plan assets – actuarially calculated – of a defined benefit, cost sharing multi-employer plan. Changes in the net pension liability during the period are recorded as pension expense, or as deferred inflows of resources or deferred outflows of resources, depending on the nature of the change, in the period incurred. Those changes in net pension liability that are recorded as deferred inflows of resources or as deferred outflows of resources, that arise from changes in actuarial assumptions or other inputs and differences between expected or actual experience, are amortized over the weighted-average remaining service life of all participants in the qualified pension plan and recorded as a component of pension expense beginning with the period in which they are incurred. Projected earnings on qualified pension plan investments are recognized as a component of pension expense. Differences between projected and actual investment earnings are reported as deferred inflows of resources or deferred outflows of resources and amortized as a component of pension expense on a closed basis over a five-year period beginning with the period in which the difference occurred.

Retirement Plan and Benefits

PNCC contributes to the Palau Civil Service Pension Trust Fund (the Fund), a defined benefit, cost-sharing, multi-employer pension plan established and administered by the Republic of Palau. The Fund issues a stand-alone financial report which is available at its office site. The Fund provides retirement, security and other benefits to employees, and their spouses and dependents, of the Republic of Palau State Governments and Republic of Palau agencies, funds and public corporations, which are paid monthly and are two percent of each member's average monthly salary. Normal benefits are the credited total service up to a maximum of thirty years total service. Generally, benefits vest after three years of credited service. Members, who retire at or after age 60, or with 30 years of vesting service, are entitled to retirement benefits. On April 30, 2013, RPPL 9-2 eliminated the mandatory service retirement after thirty years of service. After December 31, 2013, no employee shall be entitled to pension benefits until reaching the age of sixty.

In accordance with the directives of RPPL 5-7, which provides that "no person who retires after October 1, 1997, may receive benefits under the Plan unless he or she has contributed to the Plan for at least five years or has made actuarially equivalent lump sum contributions". In accordance with RPPL 9-2, members who retire after April 30, 2013 must not receive benefits greater than thirty thousand dollars per year.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Retirement Plan and Benefits, continued

Further, the amount of benefits that a member receives should not be recalculated if the member is re-employed after the member begins receiving benefits under the Fund. Additionally, a member should not receive benefits during the time the member is re-employed subsequent to retirement.

Republic of Palau Public Law (RPPL) 2-26 is the authority under which benefit provisions and contributions rates are established. Member contribution rates are established by RPPL 2-26 at six percent (6%) of total payroll and are deducted from the member dollar for dollar by the employer. Under the provisions of RPPL 2-26, the Fund's Board of Trustees adopted a Trust Fund Operation which has the force and effect of law, and which sets forth the procedures for the administration and coverage of the Plan. Amendments to the Plan are subject to the requirements of Title 6 of the Palau National Code.

RPPL 10-8 and RPPL 10-12 was effective October 1, 2018 to increase the new rate of contribution for social security from 6% to 7%. Member contribution rates are established by RPPL 10-8 and RPPL 10-12 at seven percent (7%) of total payroll and are deducted from the member dollar for dollar by the employer. Under the provisions of RPPL 10-8 and RPPL 10-12, the Fund's Board of Trustees adopted a Trust Fund Operation which has the force and effect of law, and which sets forth the procedures for the administration and coverage of the Plan. Amendments to the Plan are subject to the requirements of Title 6 of the Palau National Code.

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation of all assumptions as of September 30, 2019, for the same measurement date, using the following assumptions:

Actuarial Cost Method:	Normal costs are calculated under the entry age normal method
Amortization Method:	Level dollar, open with remaining amortization period of 30 years
Asset Valuation Method:	Market Value of Assets
Investment Income:	6.74% per year, net of investment expenses, including price inflation
Price Inflation:	2.5%

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Actuarial Assumptions, continued

Interest on Members Contribution:	5% per year
Salary Increase:	3% per year
Expenses:	$300,000 added to normal cost
Mortality:	RP 2000 Combined Mortality Table, set forward four years for all members except disability recipients, where the table is set forward ten years.
Termination of Employment:	5% for ages 20 to 39, 0% for all other ages.

Disability:

Age	Disability
25	0.21%
30	0.18%
35	0.25%
40	0.35%
45	0.50%
50	0.76%
55	1.43%
60	2.12%

Retirement Age:	100% at age 60
Form of Payment:	Single: Straight life annuity; Married: 100% joint and survivor
Marriage Assumption:	80% of the workers are assumed to be married and males are assumed to be 3 years older than their spouses. Beneficiaries are assumed to be the opposite gender of the member.
Duty vs Non-Duty Related Disability:	100% duty related
Refund of Contributions:	80% terminated vested members elect a refund of contributions

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Actuarial Assumptions, continued

Final Average Earnings:	Deferred vested members missing data for their final average earnings are assumed to have earned the average amount of current deferred vested members.
Benefits:	Retirees and beneficiaries missing data for their monthly benefit amount is assumed to receive the average benefit of current retirees or beneficiaries, respectively.

The pension benefit obligation, which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and any step-rate benefits, estimated to be payable in the future as a result of employment service to date.

The measure is intended to assist users in evaluating the Fund’s funding status on a going-concern basis, and evaluate progress made in accumulating adequate assets to pay benefits when due.

Investment Rate of Return

The long-term expected rate of return on the Fund’s investment of 6.74% was determined using log-normal distribution analysis, creating a best-estimate range for each asset class.

As of September 30, 2019 (the measurement date), the arithmetic real rates of return for each major investment class are as follows:

Assets Class	Target Allocation	Expected Rate of Return
US Large Cap Value Equity	10%	8.70%
US Large Cap Growth Equity	10%	9.13%
International Equity	15%	9.19%
Emerging Markets	10%	12.52%
US Aggregate Fixed Income	35%	3.82%
Global Broad Fixed Income	10%	3.40%
Global REIT	10%	8.33%

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Actuarial Assumptions, continued

Discount Rate

The discount rate used to measure the total pension liability was 2.85% at the current measurement date and 4.16% at the prior measurement date. The discount rate was determined using the current assumed rate of return until the point where the plan fiduciary net position is negative. Using the current contribution rates, a negative position happens in 2024 for the 2019 measurement date. For years on or after 2024, a discount rate of 2.81% is used. This rate is based on the Bond Buyer General Obligation 20-year Municipal Bond Index Rate.

Sensitivity of Net Pension Liability to Changes in the Discount Rate

The following schedule presents PNCC's proportionate share of the net pension liability as of September 30, 2019, calculated using the discount rate of 2.85%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1% lower (1.85%) or 1% higher (3.85%) from the current rate.

	1% Decrease in Discount Rate 1.85%	Current Discount Rate 2.85%	1% Increase in Discount Rate 3.85%
Net Pension Liability	$ 13,771,863	$ 11,837,827	$ 10,237,999

Deferred Outflows and Inflows of Resources

At December 31, 2020 and 2019, PNCC reported total deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	2020		2019	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 601,998	$ 461,505	$ 687,051	$ 130,099
Net difference between projected and actual earnings on pension plan investments	32,922	28,100	24,798	37,966
Change in assumptions	2,456,732	1,079,198	778,982	1,202,564
PNCC contributions subsequent to the measurement date	-	-	-	-
Changes in proportion and difference between the Authority contributions and proportionate shares of contributions	1,192,813	207,091	509,645	404,192
Total	$ 4,284,465	$ 1,775,894	$ 2,000,476	$ 1,774,821

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Deferred outflows resulting from contributions subsequent to measurement date will be recognized as reduction of the net pension liability in the following year. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions at December 31, 2020 will be recognized in pension expense as follows:

Year ending December 31,	
2021	$ 437,831
2022	454,925
2023	505,444
2024	381,918
2025	336,224
Thereafter	392,229
	$ 2,508,571

Medical and Life Insurance Benefit

In April 2010, the Republic of Palau (ROP) enacted RPPL 8-14 "*The National Healthcare Financing Act".* The law requires each resident in the Republic of Palau to have coverage for healthcare costs. The law establishes a national Medical Savings Fund and a Health Insurance System in the ROP.

In October 2010, in compliance with the requirements of RPPL 8-14, PNCC began withholding from its employees 2.5% of gross earnings each pay period, with a matching employer share (a 5% combined contribution) for remittance to the ROP Social Security Administration that administers the Medical Savings Fund and Palau Health Insurance. For the years ended December 31, 2020, 2019 and 2018, PNCC's employer's share paid to the Social Security Administration for these costs was $249,210, $239,844 and $213,423, respectively, and is included as a component of payroll burden in the Schedule of Functional Expenses.

Taxes

Based on the enactment of RPPL 1-40, PNCC is exempt from all national and state non-payroll taxes or fees. In accordance with RPPL 10-17 Telecommunications Regulatory Framework, the Bureau of Revenue and Taxation will be collecting 15% of gross revenue from any company providing telecommunications service in the Republic of Palau. This collection will be deposited into a restricted account, for payment pursuant to PNC Title 15, § 437. RPPL 10-17 has an effective date of March 1, 2018. Pursuant to RPPL 10-17, the Republic will assume the scheduled monthly payment to REA/RUS which is effective March 1, 2018.

(2) Summary of Significant Accounting Policies, continued

F. Assets, Liabilities and Net Position, continued

Taxes, continued

In accordance with RPPL 10-17, PNCC shall continue to be a Public Corporation and shall be subject to the corporate laws of the Republic. Effective January 1, 2018, PNCC is subject to 4% gross revenue taxes. “Gross revenue tax” is 4% on the total gross of all business revenues or total sums of all receipts from sources within the Republic whether in the form of cash or property derived from business, from the exploitation of capital whether in the form of receipts from the disposition of capital assets, interests, dividends, royalties, rentals, fees or otherwise, however, such receipts may be labeled without deduction or offset of any kind or nature.

Operating and Non-operating Revenues and Expenses

PNCC’s Statements of Revenues, Expenses and Changes in Net Position distinguishes between operating and non-operating revenues and expenses. Operating revenues and expenses result from exchange transactions associated directly from the operation and maintenance of telecommunication services and equipment, cellular telecommunication operations, DTV operations, and Palaunet operation services. Nonexchange revenues and expenses resulting from nonrecurring income and costs such as interest income and expense are reported as non-operating revenues.

Net Position

Net position is the residual of assets and deferred outflows of resources over liabilities and deferred inflows of resources in a statement of financial position. At December 31, 2019, PNCC’s net position is a negative $149,371, meaning that total assets exceeded total liabilities. Net position consists of three components: net investment in capital assets net of related debt; restricted - expendable and nonexpendable; and unrestricted. Net investment in capital assets component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of the related debt. Net position is reported as restricted when constraints are imposed by third parties or enabling legislation. At December 31, 2020, PNCC had a negative net position totaling $1,668,825.

When program expenses are incurred, where there are both restricted and unrestricted resources available to finance the program, expenses are first applied to restricted resources before using unrestricted resources.

(3) Deposits and Investments Risk

Deposits

GASB Statement No. 3 requires government entities to categorize deposits to give an indication of the level of credit risk assumed by the entity at year-end based on the following categories:

Category 1 - deposits that are federally insured or collateralized with securities held by PNCC or by its agent in PNCC's name;

Category 2 - deposits that are uninsured but fully collateralized with securities held by the pledging financial institution's trust department or agent in PNCC's name; or

Category 3 - deposits that are collateralized with securities held by the pledging financial institution's trust department or agent but not in PNCC's name and non-collateralized deposits.

At December 31, 2020 and 2019, the carrying amount of PNCC's cash balances was $465,082 and $296,738, respectively. The corresponding bank balances as of December 31, 2020 and 2019 were $487,590 and $532,937, respectively. From these deposits, $237,444 and $412,299, respectively, were subject to coverage by the Federal Deposit Insurance Corporation (FDIC) with the remaining balance exceeding insurable limits. PNCC does not require collateralization of bank accounts, and therefore, deposits in excess of FDIC insurance coverage are uncollateralized.

Investments

Governmental accounting standards require that the investments reported as of the balance sheet date be categorized according to level of credit risk. The level of credit risk is defined as follows:

Category 1 - insured and registered for which the securities are held by PNCC or by its agent in PNCC's name;

Category 2 - uninsured and registered for which the securities are held by the broker's or dealer's trust department or agent in PNCC's name; and

Category 3 - uninsured and unregistered for which the securities are held by the broker or dealer or by its trust department or agent but not in PNCC's name.

(3) Deposits and Investments Risk, continued

Fair Value Measurement of the Investments

Investment and related investment earnings are reported at fair value using quoted market prices. Fair value is the price that would be received to sell an asset paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the date as of which the fair value of an asset or liability is determined. The PNCC categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles.

The hierarchy is based on the valuation inputs used to measure the fair value of the assets. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant observable inputs; Level 3 inputs are significant unobservable inputs. PNCC has the following fair value measurements:

		Fair Value Measurement Using		
Investments by fair value level	12/31/2020	Level 1	Level 2	Level 3
Fixed income securities:				
Corporate Bonds	$ 474,576	$ -	$ 474,576	$ -
U.S. Treasury	356,623	356,623	-	-
Federal Agencies	70,719	-	70,719	-
Equity securities:				
U.S. Equities	1,204,065	1,204,065	-	-
Non-U.S. Equities	496,318	496,318	-	-
Total investments by fair value level	$ 2,602,301	$ 2,057,006	$ 545,295	$ -
Investments measured at net asset value (NAV):				
Exchanged-traded funds	$ 29,882			
Investments measured at cost based measure:				
Money market funds	$ 79,941			
Total investments	$ 2,712,124			

(3) Deposits and Investments Risk, continued

Fair Value Measurement of the Investments, continued

		Fair Value Measurement Using		
Investments by fair value level	12/31/2019	Level 1	Level 2	Level 3
Fixed income securities:				
Corporate Bonds	$ 256,129	$ -	$ 256,129	$ -
U.S. Treasury	307,765	307,765	-	-
Federal Agencies	70,442	-	70,442	-
Equity securities:				
U.S. Equities	1,084,607	1,084,607	-	-
Non-U.S. Equities	225,014	225,014	-	-
Total investments by fair value level	$ 1,943,957	$ 1,617,386	$ 326,571	$ -
Investments measured at net asset value (NAV):				
Exchanged-traded funds	$ 36,315			
Investments measured at cost based measure:				
Money market funds	$ 242,478			
Total investments	$ 2,222,750			

Restricted Cash and Cash Equivalents

PNCC's restricted cash and cash equivalents must comply with Section 22 of the Pledge of Assets and Agreement to Create Trust (Rural Electrification Administration "REA" Loan Agreement), wherein PNCC is required to maintain a funded reserve in such amount that the balance of the funds covered by the First Note shall at no time be less than the outstanding principal and unpaid interest of the First Note. The reserve shall be maintained in accordance with a plan submitted to and approved in writing by the Administrator of REA (now the Rural Utilities Service or "RUS").

The balance of the reserve shall comply with the abovementioned Section 22 no later than one year from the date of this first advance of funds covered by the First Note. Thereafter, PNCC must maintain such compliance continuously. Assets held in the reserve must be held by a bank or institution or other depository whose funds are insured by the Federal government and shall consist of (a) Federal government securities held in PNCC's name; (b) other securities by an institution whose senior unsecured debt obligations are rated in any of the top three categories by a nationally recognized rating organization; or (c) cash. All of PNCC's restricted cash and cash equivalents with a market value of $250,146 and $250,113 as of December 31, 2020 and 2019, respectively, were deposited in FDIC insured financial institutions.

(3) Deposits and Investments Risk, continued

Fair Value Measurement of the Investments, continued

On December 31, 2015, PNCC's Emergency Reserve Fund (the Fund) has been invested with Raymond James as the new investment consultant, which holds the investments in PNCC's name. The PNCC's Board of Directors is responsible for directing and monitoring the investment management of the Fund. The Board of Directors currently has no specific projected contribution or distribution requirements for the Fund. The Board of Directors shall, from time to time, designate accumulated reserves to be contributed to and managed under the auspices of the Fund. The Fund will be invested in such a way that adequate funds can be made available within a short period of time, should a distribution need arise.

At December 31, 2020 and 2019, PNCC's investment portfolios at fair value are as follows:

	2020			2019		
	Allocation		Market	Allocation		Market
	Actual	Policy	Value	Actual	Policy	Value
Fixed income securities:						
Corporate Bonds			$ 474,576			$ 256,129
U.S. Treasury			356,623			307,765
Federal Agencies			70,719			70,442
Total fixed income	33%	36%	901,918	29%	36%	634,336
Equity securities:						
U.S. Equities	45%	43%	1,204,065	49%	43%	1,084,607
Non-U.S. Equities	18%	19%	496,318	10%	19%	225,014
Total equity securities			1,700,383			1,309,621
Exchange-traded funds	1%	1%	29,882	1%	1%	36,315
Cash and cash equivalents	3%	1%	79,941	11%	1%	242,478
Total investments	100%	100%	$ 2,712,124	100%	100%	$ 2,222,750

(3) Deposits and Investments Risk, continued

Fair Value Measurement of the Investments, continued

At December 31, 2020 and 2019, PNCC's fixed income securities had the following ratings and maturities:

As of December 31, 2020

		Investment maturities (in years)				Rating	
Investment type	Fair Value	Less than 1	1-5	6-10	More than 10	Moody	Standard & Poor
Corporate bonds	$ 27,431	$ -	$ -	$ 27,431	$ -	Baa2	BBB
Corporate bonds	27,200	-	-	27,200	-	A2	A-
Corporate bonds	27,786	-	-	27,786	-	Baa3	BBB
Corporate bonds	27,369	-	-	27,369	-	Baa2	BBB
Corporate bonds	27,805	-	-	27,805	-	Baa3	BBB
Corporate bonds	27,652	-	-	27,652	-	A3	A-
Corporate bonds	27,687	-	-	27,687	-	A3	A-
Corporate bonds	28,130	-	-	28,130	-	Baa2	BBB
Corporate bonds	27,389	-	-	27,389	-	Baa2	BBB
Corporate bonds	29,737	-	-	29,737	-	Baa1	BBB
Corporate bonds	27,981	-	-	27,981	-	A2	A-
Corporate bonds	27,993	-	-	27,993	-	Baa2	BBB
Corporate bonds	27,418	-	-	-	27,418	Aaa	AAA
Corporate bonds	28,425	-	-	-	28,425	Baa1	BBB+
Corporate bonds	28,006	-	-	28,006	-	A3	A-
Corporate bonds	28,868	-	-	-	28,868	Baa2	BBB
Corporate bonds	27,699	-	-	27,699	-	A2	BBB+
Federal agencies	70,719	-	70,719	-	-	Aaa	AA+
U.S. Treasury	45,298	-	-	-	45,298	Aaa	No rating
U.S. Treasury	35,358	-	-	-	35,358	Aaa	No rating
U.S. Treasury	46,344	-	-	46,344	-	Aaa	No rating
U.S. Treasury	27,419	-	-	27,419	-	Aaa	No rating
U.S. Treasury	37,129	-	37,129	-	-	Aaa	No rating
U.S. Treasury	46,425	-	-	46,425	-	Aaa	No rating
U.S. Treasury	45,024	-	45,024	-	-	Aaa	No rating
U.S. Treasury	27,626	-	27,626	-	-	Aaa	No rating
U.S. Treasury	46,000	-	-	46,000	-	Aaa	No rating
Total	$ 901,918	$ -	$ 180,498	$ 556,053	$ 165,367		

(3) Deposits and Investments Risk, continued

Fair Value Measurement of the Investments, continued

As of December 31, 2019

		Investment maturities (in years)				Rating	
Investment type	Fair Value	Less than 1	1-5	6-10	More than 10	Moody	Standard & Poor
Corporate bonds	$ 20,025	$ -	$ -	$ 20,025	$ -	Baa2	BBB
Corporate bonds	19,668	-	-	19,668	-	A3	A-
Corporate bonds	19,280	-	-	19,280	-	A2	A
Corporate bonds	20,207	-	-	20,207	-	A2	A-
Corporate bonds	19,928	-	-	19,928	-	Baa3	BBB
Corporate bonds	19,664	-	-	19,664	-	Baa2	BBB
Corporate bonds	19,528	-	-	19,528	-	A3	A-
Corporate bonds	19,148	-	-	19,148	-	A3	A-
Corporate bonds	19,162	-	-	19,162	-	A3	BBB+
Corporate bonds	20,000	-	-	20,000	-	A2	A-
Corporate bonds	19,090	-	-	19,090	-	Baa2	BBB
Corporate bonds	19,931	-	-	-	19,931	Baa1	A-
Corporate bonds	20,498	-	-	20,498	-	A2	A-
Federal agencies	51,149	-	51,149	-	-	Aaa	AA+
Federal agencies	19,293	-	19,293	-	-	Aaa	AA+
U.S. Treasury	39,102	-	-	-	39,102	Aaa	No rating
U.S. Treasury	30,410	-	-	-	30,410	Aaa	No rating
U.S. Treasury	32,312	-	-	32,312	-	Aaa	No rating
U.S. Treasury	33,246	-	33,246	-	-	Aaa	No rating
U.S. Treasury	25,681	-	-	25,681	-	Aaa	No rating
U.S. Treasury	31,871	-	-	31,871	-	Aaa	No rating
U.S. Treasury	18,539	-	-	18,539	-	Aaa	No rating
U.S. Treasury	25,162	-	25,162	-	-	Aaa	No rating
U.S. Treasury	32,444	-	-	32,444	-	Aaa	No rating
U.S. Treasury	38,998	-	-	38,998	-	Aaa	No rating
Total	$ 634,336	$ -	$ 128,850	$ 416,043	$ 89,443		

(4) Capital Assets

PNCC's capital assets for the years ended December 31, 2020 and 2019 are summarized below as follows:

	Balance at December 31, 2019	Additions	Transfers/ Retirements	Balance at December 31, 2020
Regulated capital assets				
Cables and transmission lines	$ 28,009,294	$ 465,119	$ -	$ 28,474,413
Transmission equipment	9,749,475	-	-	9,749,475
Buildings	10,005,059	4,188	-	10,009,247
Central office equipment	3,504,117	1,066,579	-	4,570,696
General support equipment	2,454,836	264,366	-	2,719,202
Customer premises wiring and equipment	1,456,018	113,709	-	1,569,727
Vehicles	823,053	24,095	-	847,148
Furniture and fixtures	34,013	2,793	-	36,806
Regulated capital assets, at cost	56,035,865	1,940,849	-	57,976,714
Accumulated depreciation	(44,923,306)	(1,525,711)	-	(46,449,017)
Regulated capital assets, at net book value	11,112,559	415,138	-	11,527,697
Non-regulated capital assets				
Cable television	3,526,496	130,652	-	3,657,148
Cellular	13,873,069	1,515,965	-	15,389,034
Palaunet	2,146,840	156,637	-	2,303,477
Non-regulated capital assets, at cost	19,546,405	1,803,254	-	21,349,659
Accumulated depreciation	(10,949,135)	(1,279,093)	-	(12,228,228)
Non-regulated capital assets, at net book value	8,597,270	524,161	-	9,121,431
Construction in progress	2,558,003	1,742,784	(3,744,102)	556,685
Total	$ 22,267,832	$ 2,682,083	$ (3,744,102)	$ 21,205,813

(4) Capital Assets, continued

	Balance at December 31, 2018	Additions	Transfers/ Retirements	Balance at December 31, 2019
Regulated capital assets				
Cables and transmission lines	$ 27,671,780	$ 337,514	$ -	$ 28,009,294
Transmission equipment	9,749,475	-	-	9,749,475
Buildings	9,604,850	400,209	-	10,005,059
Central office equipment	3,102,624	401,493	-	3,504,117
General support equipment	2,374,435	80,401	-	2,454,836
Customer premises wiring and equipment	1,454,858	1,160	-	1,456,018
Vehicles	700,253	122,800	-	823,053
Furniture and fixtures	34,013	-	-	34,013
Regulated capital assets, at cost	54,692,288	1,343,577	-	56,035,865
Accumulated depreciation	(43,474,514)	(1,448,792)	-	(44,923,306)
Regulated capital assets, at net book value	11,217,774	(105,215)	-	11,112,559
Non-regulated capital assets				
Cable television	3,294,326	232,170	-	3,526,496
Cellular	13,787,335	85,734	-	13,873,069
Palaunet	1,984,071	162,769	-	2,146,840
Non-regulated capital assets, at cost	19,065,732	480,673	-	19,546,405
Accumulated depreciation	(9,728,745)	(1,220,390)	-	(10,949,135)
Non-regulated capital assets, at net book value	9,336,987	(739,717)	-	8,597,270
Construction in progress	1,340,744	3,041,510	(1,824,251)	2,558,003
Total	$ 21,895,505	$ 2,196,578	$ (1,824,251)	$ 22,267,832

Depreciation expense for the years ended December 31, 2020 and 2019 was $2,804,804 and $2,669,183, respectively, and is reported in the Statements of Revenues, Expenses and Changes in Net Position.

(5) Related Party Transactions

In the ordinary course of business, PNCC provides local and long distance telephone services, cellular telecommunications services and equipment, digital cable television services, and internet services, to the National government of the Republic of Palau and its component units. These services are provided at the same service rates and delinquent fees charged to all third-party customers. As of December 31, 2020 and 2019, amounts due from the Republic of Palau and its component units totaled $391,212 and $729,230, respectively.

(6) Long-term Debt

Long-term debt as of December 31, 2020 and 2019 are summarized below:

	2020	2019
Mortgage note payable to Rural Utilities Services (RUS) at 4.59% per annum, payable in monthly installments of $192,181, and due October 2029. The note is collateralized by substantially all of PNCC's assets and a pledge of its revenues.	$ 16,593,735	$ 17,371,069
Less current portion	2,357,943	1,531,736
Long-term debt, net of current portion	$ 14,235,792	$ 15,839,333

RUS Mortgage Note

The original RUS note of $39,143,000 approved in 1992 was unconditionally guaranteed by ROP and stipulates that ROP will make debt service payments to RUS in the event of default. On April 8, 2009, RUS approved the request of PNCC to rescind the remaining balance of $395,047 of the mortgage note which had not been advanced. The RUS Mortgage and Security Agreement sets out certain financial ratios that must be met before a dividend can be declared. If these ratios are not met, dividends may only be declared with a written approval of RUS.

On July 31, 2020, PNCC entered into a Deferral Agreement with RUS. Principal payments were deferred for 12 months commencing July 2020 and PNCC is only required to interest payments for that period. After the principal deferment period July 2021, PNCC will resume monthly principal and interest payments until maturity. The principal amount deferred will be re-amortized after the deferment period. The negative loan covenants require PNCC to submit monthly and quarterly financials, monthly billings and collection reports, balances of accounts receivable and accounts payable, and the number of customers by service offering type. PNCC is not allowed to issue bonuses or increments during the deferment period.

The management of PNCC believes it is in compliance with the RUS mortgage loan covenants at December 31, 2020 and 2019.

(6) Long-term Debt, continued

Future minimum principal and interest payments for the RUS mortgage are as follows:

Years ending December 31,	Principal	Interest	Total
2021	$ 2,357,943	$ 702,635	$ 3,060,578
2022	1,678,708	627,464	2,306,172
2023	1,757,402	548,770	2,306,172
2024	1,839,789	466,386	2,306,175
2025	1,926,034	380,141	2,306,175
2026-2029	7,033,859	951,420	7,985,279
	$ 16,593,735	$ 3,676,816	$ 20,270,551

At December 31, 2020 and 2019, the changes in the long-term liabilities are as follows:

	Balance January 1, 2020	Additions	Reductions	Balance December 31, 2020	Current	Noncurrent
Rural Utilities Services	$ 17,371,069	$ -	$ 777,334	$ 16,593,735	$ 2,357,943	$ 14,235,792
Net Pension Liability	8,712,379	3,125,448	-	11,837,827	-	11,837,827
	$ 26,083,448	$ 3,125,448	$ 777,334	$ 28,431,562	$ 2,357,943	$ 26,073,619

	Balance January 1, 2019	Additions	Reductions	Balance December 31, 2019	Current	Noncurrent
Rural Utilities Services	$ 18,836,699	$ -	$ 1,465,630	$ 17,371,069	$ 1,531,736	$ 15,839,333
Net Pension Liability	8,539,634	172,745	-	8,712,379	-	8,712,379
	$ 27,376,333	$ 172,745	$ 1,465,630	$ 26,083,448	$ 1,531,736	$ 24,551,712

Interest expense paid in 2020 and 2019 amounted to $770,106 and $840,515, respectively.

(7) Commitments and Contingencies

Commitments

PNCC entered into an equipment purchase agreement for the installation of equipment and upgrade of Fourth Generation (4G) and (3G) Network (NodeB) plus LTE license for multiple modes of additional 1800MHz – 2100Mhz. Under this agreement, PNCC agreed to purchase the equipment and installations of accessories for the required upgrade total of $374,540. The contract calls for a down payments of 50% or $187,270 on or before December 31, 2019.

The remaining balance is to be paid in six months at $31,212 per month from January 1, 2020 to July 30, 2020. Interest will be applied to the unpaid balance at the rate of 2% per annum. As of December 31, 2020, PNCC had paid $312,117 to the vendor under this contract. Since the equipment installation upgrade is still in progress, the payment has been recognized as prepaids to the contractor. At December 31, 2020, future payments under this contract were $62,423.

The Company entered in a five-year lease agreement effective May 24, 2019 and expiring May 23, 2024. The Company was required to make an advance payment of $200,000, then commencing on the third year, the Company is required to make payments of $12,000 per month payable in advance by no later than the 10th day of each month.

The Company has a lease on a land easement agreement effective of May 21, 2019 and expiring May 20, 2024. The agreement calls for monthly payments of $182. Rent under this lease is recognized at $2,220 per year.

The Company has a lease on a land easement agreement effective of March 1, 2019 and expiring March 1, 2024. The agreement calls for monthly payments of $700. Rent under this lease is recognized at $8,400 per year.

The Company has a lease on a land easement agreement effective of March 1, 2019 and expiring March 1, 2024. The agreement calls for monthly payments of $700. Rent under this lease is recognized at $8,400 per year.

The Company has a lease on a land easement agreement effective of August 8, 2019 and expiring August 7, 2027. The agreement calls for monthly payments of $1,000. Rent under this lease is recognized at $12,000 per year.

The Company entered into a five-year network equipment maintenance agreement effective March 1, 2019 and expiring March 1, 2024. The agreement calls for annual commitments of $2,980.

(7) Commitments and Contingencies, continued

The Company entered into a three-year broadcast connectivity agreement effective October 14, 2019 and expiring October 14, 2022. The agreement calls for quarterly payments of $540. The service fee is recognized at $2,160 per year.

The Company entered into a three-year broadcast connectivity agreement effective August 22, 2019 and expiring August 22, 2022. The agreement calls for monthly payments of $287. The service fee is recognized at $3,444 per year.

The Company entered into a three-year broadcast connectivity agreement effective August 16, 2019 and expiring August 15, 2022. The agreement calls for monthly payments of $287. The service fee is recognized at $3,444 per year.

The Company entered into a three-year broadcast connectivity agreement effective December 12, 2019 and expiring December 11, 2022. The agreement calls for monthly payments of $287. The service fee is recognized at $3,444 per year.

The Company entered into a broadcaster licensing agreement effective September 1, 2019 and expiring June 30, 2022. The agreement calls for an annual payment of $500.

The Company entered into a security service agreement effective April 1, 2019 and expiring May 31, 2021. The agreement calls for monthly payments of $5,425. The service fee is recognized at $65,100 per year.

Future minimum lease and services payments were as follows:

2021	$ 208,000
2022	178,000
2023	168,000
2024	75,000
2025	12,000
Thereafter	20,000
	$ 661,000

(7) Commitments and Contingencies, continued

Contingencies

Risk Management

PNCC is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; errors and omissions; employee injuries and illnesses; natural disasters, employee health, dental and accident benefits. PNCC has elected to purchase commercial insurance coverage for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the past three years. PNCC is self-insured for buried cables and customer premises wirings.

Claims expenditures and liabilities will be reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Losses, if reported, would include an estimate of claims that have been incurred but not reported. No losses as a result of these risks have occurred or have been reported within the last three years.

Claims and Litigation

In the normal course of business, PNCC is involved in various claims and litigation or has received several claims that are pending review or are expected to go to litigation. Management believes that any liability it may incur would not have a material adverse effect on its financial condition or its results of operations.

Health (Sick) Leave

PNCC's policy is to record expenditures for health (sick) leave when the leave is actually taken. Sick leave is compensated time for absence during working hours arising from employee illness or injury. The estimated accumulated sick leave at December 31, 2020 and 2019 was $1,287,818 and $1,216,774 respectively.

(8) 401(k) Profit Sharing Plan

PNCC has adopted a retirement plan (a "401(k) plan) which covers substantially all employees meeting certain eligibility requirements. Participants may contribute a portion of their pretax income into a retirement fund. At the Company's discretion, participants' contributions are matched up to 5% by the Company. For the years ended December 31, 2020 and 2019, the Company's discretionary profit-sharing contribution were $44,683 and $33,152, respectively. The contributions are recorded as a component of plant specific operations expenses reported in the Statement of Revenues, Expenses and Changes in net position.

(9) Fair Value of Financial Instruments

PNCC's financial instruments are cash and cash equivalents, accounts receivable, other assets, investments, accounts payable, payable to carriers, accrued expenses, unearned revenue, customer deposits, notes payable, and long-term debt. The recorded values of these instruments for cash and cash equivalents, accounts receivable, other assets, investments and accounts payable, payable to carriers, accrued expenses, unearned revenues, and the current portion of long-term debt approximate their fair values based on their short-term nature. The recorded value of customer deposits approximates its fair value as the amount payable on demand at the reporting date. The recorded value of RUS note payable approximates its fair value, as interest approximates market rates.

(10) Reclassifications

Certain amounts presented in 2019 have been reclassified to conform to the 2020 financial statement presentation. These reclassifications did not affect the change in net position or the total net position.

(11) COVID-19

In December 2019, an outbreak of a novel strain of coronavirus (COVID-19) originated in Wuhan, China and has since spread to other countries, including the U.S and throughout Micronesia. On March 11, 2020, the World Health Organization characterized COVID-19 as a pandemic. In addition, multiple jurisdictions in the U.S. have declared a state of emergency. It is anticipated that these impacts will continue for some time. Future potential impacts may include disruptions on the Company's employees' ability to work or the customers' ability to pay monthly services. Changes to the operating environment may increase operating costs. Additional impacts may include the ability of customers to continue making payments as a result of job loss or other pandemic related issues. The future effects of these issues are unknown.

(12) Subsequent Event

PNCC has evaluated subsequent events through July 30, 2021, the date the financial statements were available to be issued. There were no such events requiring disclosure.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

SUPLEMENTARY SCHEDULES

Year Ended December 31, 2020

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Supplementary Information
Schedule of Budget vs Actual (GAAP Basis)
For the Year Ended December 31, 2020

	Budget				Variance Favorable
	Original	Revisions	Final	Actual	(Unfavorable)
Operating revenues:					
Cellular	$ 6,221,618	$ -	$ 6,221,618	$ 6,189,716	$ (31,902)
Palaunet	2,654,502	-	2,654,502	3,129,431	474,929
Digital television	1,219,051	-	1,219,051	1,227,625	8,574
Local	1,418,784	(425,635)	993,149	1,700,249	707,100
Long distance	199,105	(59,732)	139,373	(16,391)	(155,764)
Miscellaneous	309,155	(92,747)	216,408	142,446	(73,962)
Provision for doubtful accounts	-	-	-	(104,816)	(104,816)
Total operating revenues	12,022,215	(578,114)	11,444,101	12,268,260	824,159
Operating expenses:					
Plant specific operations	5,422,168	(1,084,434)	4,337,734	5,500,240	(1,162,506)
Depreciation	2,328,761	(465,752)	1,863,009	2,804,804	(941,795)
Customer service operations	1,465,541	(293,108)	1,172,433	1,629,054	(456,621)
Corporate operations	2,231,709	(446,342)	1,785,367	2,754,262	(968,895)
Plant non-specific operations	601,232	(120,247)	480,985	854,868	(373,883)
Total operating expenses	12,049,411	(2,409,883)	9,639,528	13,543,228	(3,903,700)
Operating income	(27,196)	1,831,769	1,804,573	(1,274,968)	(3,079,541)
Non-operating income (expenses):					
Interest expense	(914,311)	182,863	(731,448)	(770,106)	(38,658)
Unrealized gain on investment	-	-	-	527,520	527,520
Realized gain on investments	(72,483)	14,497	(57,986)	-	57,986
Non-operating income	-	-	-	-	-
Income on investment	-	-	-	-	-
Gain (loss) on disposal of equipment	-	-	-	-	-
Other expense	(55,750)	11,150	(44,600)	(1,900)	42,700
Total nonoperating expenses, net	(1,042,544)	208,510	(834,034)	(244,486)	589,548
Change in net position	$ (1,069,740)	$ 2,040,279	$ 970,539	$ (1,519,454)	$ (2,489,993)

See accompanying independent auditor's report.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Supplementary Schedule of Functional Expenses
For The Year Ended December 31, 2020
(With Comparative Totals for 2019)

	Plant Specific					Plant	Total	
				Customer		Non-Specific	Operating Expenses	
	Depreciation	Operations	Corporate	Relations	Total	Operations	2020	2019
Outside services	$ -	$ 3,468,744	$ 250,697	$ 697,885	$ 4,417,326	$ 1,776	$ 4,419,102	$ 5,136,017
Depreciation	2,804,804	-	-	-	2,804,804	-	2,804,804	2,669,183
Others	-	631,275	303,691	160,378	1,095,344	276,783	1,372,127	784,873
Salaries and wages	-	-	653,444	476,923	1,130,367	231,203	1,361,570	3,001,890
Utilities	-	570,248	-	-	570,248	27,104	597,352	657,690
Materials and supplies	-	569,309	2,029	3,335	574,673	17,533	592,206	207,689
Bad debts	-	-	504,756	-	504,756	-	504,756	-
Gross revenue taxes	-	-	456,737	-	456,737	-	456,737	493,386
Clearance	-	196,748	-	-	196,748	216	196,964	41,835
Insurance	-	-	143,909	-	143,909	-	143,909	86,924
Legal fees	-	-	59,580	-	59,580	-	59,580	57,641
Fuel	-	46,230	11,794	-	58,024	20	58,044	80,856
Training	-	17,483	17,753	3,253	38,489	2,786	41,275	252,056
Office supplies	-	203	30,707	6,436	37,346	2,989	40,335	52,621
Postage	-	-	30,849	-	30,849	-	30,849	20,413
Payroll burden	-	-	280,844	280,844	561,688	294,458	856,146	545,689
Board fees	-	-	7,472	-	7,472	-	7,472	9,207
Rent	-	-	-	-	-	-	-	-
Allocation	-	-	-	-	-	-	-	(1)
	$ 2,804,804	$ 5,500,240	$ 2,754,262	$ 1,629,054	$ 12,688,360	$ 854,868	$ 13,543,228	$ 14,097,969

See accompanying independent auditor's report.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Supplementary Schedule of Functional Expenses by Division
For The Year Ended December 31, 2020
(With Comparative Totals for 2019)

	Depreciation	Operations	Corporate	Customer Relations	Total Operating Expenses By Division 2020	Total Operating Expenses By Division 2019
Telephony:						
Outside services	$ -	$ 2,738,687	$ 250,697	$ 51,181	$ 3,040,565	$ 2,588,078
Depreciation	1,525,711	-	-	-	1,525,711	1,448,792
Salaries and wages	-	-	653,444	476,923	1,130,367	1,951,984
Others	-	202,335	303,691	116,902	622,928	677,750
Utilities	-	570,248	-	-	570,248	657,690
Bad debts	-	-	504,756	-	504,756	-
Business gross revenue tax	-	-	456,737	-	456,737	493,386
Materials and supplies	-	234,784	2,029	3,335	240,148	128,388
Clearance	-	197,848	-	-	197,848	32,484
Insurance	-	-	143,909	-	143,909	86,924
Legal fees	-	-	59,580	-	59,580	57,641
Fuel	-	34,836	11,794	-	46,630	70,273
Office supplies		117	30,707	6,436	37,260	46,948
Postage	-	-	30,849	-	30,849	20,413
Training	-	9,232	17,753	3,253	30,238	232,295
Board fees	-	-	7,472	-	7,472	9,207
Payroll burden	-	-	280,844	280,844	561,688	331,436
Allocation	-	-	-	-	-	(9,099)
	1,525,711	3,988,087	2,754,262	938,874	9,206,934	8,824,590
Cellular:						
Depreciation	884,634	-	-	-	884,634	880,153
Outside services	-	80,512	-	-	80,512	86,518
Others	-	24,289	-	42,000	66,289	70,992
Materials and supplies	-	1,875	-	-	1,875	4,577
Training	-	343	-	-	343	1,327
Salaries and wages	-	-	-	-	-	86,793
Payroll burden	-	-	-	-	-	402
Allocation	-	-	-	-	-	4,964
	884,634	107,019	-	42,000	1,033,653	1,135,726
Palaunet:						
Outside services	-	649,545	-	-	649,545	1,676,700
Others	-	215,698	-	-	215,698	2,421
Depreciation	176,156	-	-	-	176,156	161,713
Training	-	710	-	-	710	4,814
Materials and supplies	-	672	-	-	672	2,003
Salaries and wages	-	-	-	-	-	157,527
Payroll burden	-	-	-	-	-	54,463
Clearance	-	-	-	-	-	1,359
Allocation	-	-	-	-	-	3,238
	176,156	866,625	-	-	1,042,781	2,064,238
Digital TV:						
Outside services	-	-	-	646,704	646,704	783,709
Materials and supplies	-	331,978	-	-	331,978	42,373
Depreciation	218,303	-	-	-	218,303	178,525
Others	-	188,953	-	1,476	190,429	5,660
Fuel	-	11,394	-	-	11,394	7,754
Training	-	7,198	-	-	7,198	80
Office supplies	-	86	-	-	86	896
Clearance	-	(1,100)	-	-	(1,100)	6,915
Salaries and wages	-	-	-	-	-	429,226
Payroll burden	-	-	-	-	-	6,916
Allocation	-	-	-	-	-	896
	218,303	538,509	-	648,180	1,404,992	1,462,950
	$ 2,804,804	$ 5,500,240	$ 2,754,262	$ 1,629,054	$ 12,688,360	$ 13,487,504

See accompanying independent auditor's report.

Palau National Communications Corporation
(A Component Unit of the Republic of Palau)

Required Supplemental Information (Unaudited)
Schedule of Proportionate Share of the Net Pension Liability
Last 10 Fiscal Years*

	2019	2018	2017	2016	2015	2014
Civil Service Pension Trust Fund (Plan) total net pension liability	$ 308,480,463	$ 250,868,784	$ 259,395,005	$ 249,453,960	$ 215,546,176	$ 204,281,232
PNCC proportionate share of the net pension liability	$ 11,837,827	$ 8,712,379	$ 8,539,634	$ 7,980,506	$ 7,015,927	$ 7,163,121
PNCC proportionate share of the net pension liability	3.837%	3.473%	3.292%	3.199%	3.255%	3.506%
PNCC's covered-employee payroll**	$ 2,293,283	$ 2,037,433	$ 1,907,250	$ 1,694,398	$ 1,578,557	$ 1,648,460
PNCC's proportionate share of the net pension liability as a percentage of its covered employee payroll	516.20%	427.62%	447.75%	470.99%	444.45%	434.53%
Plan Fiduciary net position as a pencentage of the total pension liability	8.26%	10.24%	10.18%	10.55%	11.54%	14.01%

* This data is presented for those years for which information is available.
** Covered-employee payroll data from the actuarial valuation date with a one-year lag.

Palau National Communications Corporation
(A Component Unit of the Republic of Palau)

Required Supplemental Information (Unaudited)
Schedule of Pension Contributions
Last 10 Fiscal Years*

	2019	2018	2017	2016	2015	2014
Actuarially determined contribution	$ 540,730	$ 601,245	$ 565,547	$ 461,242	$ 354,787	$ 372,513
Contribution in relation to the actuarially determined contribution	137,597	122,246	114,435	100,271	94,083	97,071
Contribution (excess) deficiency	$ 403,133	$ 478,999	$ 451,112	$ 360,971	$ 260,704	$ 275,442
PNCC's covered-employee payroll**	$ 2,293,283	$ 2,037,433	$ 1,907,250	$ 1,694,398	$ 1,578,557	$ 1,648,460
PNCC's proportionate share of the net pension liability	6.00%	6.00%	6.00%	5.92%	5.96%	5.89%

* This data is presented for those years for which information is available.
** Covered-employee payroll data from the actuarial valuation date with a one-year lag.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL AND ON COMPLIANCE

Year Ended December 31, 2020

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors
Palau National Communications Corporation:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Palau National Communications Corporation (PNCC), a component unit of the Republic of Palau, as of and for the year ended December 31, 2020, and the related notes to the financial statements, which collectively comprise PNCC's basic financial statements and have issued our report thereon dated July 30, 2021.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered PNCC's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of PNCC's internal control. Accordingly, we do not express an opinion on the effectiveness of PNCC's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses and consider findings 2020-01 to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider Finding 2020-02 described in the accompany schedule of findings and responses to be significant deficiencies.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether PNCC's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

PNCC's Response to Findings

PNCC's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. PNCC's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Burger Comer Magliari

BURGER COMER MAGLIARI
Koror, Republic of Palau
July 30, 2021

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Schedule of Findings and Responses
Year Ended December 31, 2020

SECTION I – SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued:	Unmodified	

Internal control over financial reporting:

• Material weakness(es) identified?	__X__ yes	______ no
• Significant deficiency(ies) identified that are not considered to be material weaknesses?	__X__ yes	______ no
• Noncompliance material to financial statements?	______ yes	__X__ no

SECTION II – FINDINGS ON INTERNAL CONTROL OVER FINANCIAL REPORTING

CURRENT YEAR FINDINGS:

Finding No.: 2020-01
Area : Customer Deposits

Criteria:

PNCC's customer deposits consist of subscriber deposits, installation fees and amounts received for related services and subscriptions to be provided in future periods. PNCC's policy requirement of customer deposit amount varies depending on the type of service or subscription applied for. Deposits are eligible for refunding after twelve (12) consecutive months of prompt payment history. If a deposit is held on an account at the time services are terminated, the deposit will be applied to the unpaid balance and refund check is issued for the remainder. Refunds are not automatic; the customer must request a refund.

Condition:

The year-end deposit listings totaled $570,197 representing numerous inactive customer deposits over 10 years old, and whose deposits can be applied to the customer's unpaid balance.

Cause:

There is a lack of internal control monitoring procedures over the accounts receivable collection policy to determine when and how customer deposits should be applied to past-due or terminated account balances. Additionally, some customers no longer pursue request for a deposit refund because of the time and effort involved.

Effect:

The propriety of some customer deposits may not be a liability and might be a recovery of previously provided allowance for uncollectibility of accounts receivable outstanding for over 12 years.

Prior Year Status:

The lack of internal control and a formalized accounts receivable collection policy over customer deposits was cited as finding in the audit in 2013 through 2019 audits of PNCC.

SECTION II – FINDINGS ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Finding No.: 2020-01, continued
Area : Customer Deposits

Recommendation:

Management should review and revise its procedures over maintaining, accounting for and application of customer deposits in relation to accounts receivable and the allowance for doubtful accounts. Management review of this area can result in a reduction in the number and amount of delinquent and potential uncollectible accounts receivable. An in-house study should be conducted to determine to what extent, if any, deposits should be applied to the receivable allowance account. In January 2017, PNCC implemented the formal procedure by effective reviewing the customer's deposit account on a monthly basis in relation to account receivable and the allowance for doubtful accounts balances. As of December 31, 2020, the implementation of procedures is incomplete.

Auditee Response and Corrective Action Plan:

PNCC agrees with this finding and after thorough reconciliation, customer deposits will be applied to outstanding customer account balances in accordance with PNCC's Accounts Receivable Write-off policy. The CFO will ensure procedures are adhered to. The Company will keep observing the effectiveness of implemented procedures.

This is a finding is a repeat and unresolved.

SECTION II – FINDINGS ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Finding No.: 2020-02
Area : Unearned revenues from prepaid long distance sales and prepaid airtime

Criteria:

Written policies and procedures should exist to reconcile actual long-distance minutes billed by international carrier amounts to the general ledger control accounts on a monthly and year-end basis. Recognition of revenues from international prepaid calling cards/airtime should only be recognized when actual minutes are used.

Condition:

Periodic reconciliations and evaluation are not performed for long distance revenue or for prepaid international calling card and prepaid airtime based on actual minutes used. When customers do not use all of the time value of international prepaid calling card, the unused portion of the dollar value of the prepaid calling card (commonly known as breakage), may be estimated based on historical trends. At December 31, 2019, deferred revenues from unused long-distance prepaid card and wireless airtime were not calculated and recognized.

Cause:

There is a deficiency in the network system for determining unused minutes representing unearned revenue from prepaid long-distance card and prepaid airtime wireless. There also a lack of internal control policies and procedures to ensure that long distance revenues are reconciled with outbound minutes billed by international carriers on a periodic basis.

Effect:

Prepaid long-distance card sales and prepaid wireless card sales may be overstated by deferred revenues from unused minutes.

Prior Year Status:

The lack of reconciliation of actual minutes billed by international carriers and actual minutes used for prepaid airtime to revenue control totals was reported as finding in the audit of PNCC for the years 2007 through 2019.

SECTION II – FINDINGS ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Finding No.: 2020-02, continued
Area : Unearned revenues from prepaid long distance sales and prepaid airtime

Recommendation:

PNCC should document and adhere to existing policies and procedures over the reconciliation of long-distance minutes and international prepaid calling card/airtime. Minutes billed by international carriers should be reconciled to long distance revenue control on a periodic basis. Recognition of revenues from international prepaid calling cards/airtime should only be recognized when actual minutes are used. Unearned revenues should be recognized from unused prepared debusch and airtime.

Auditee Response and Corrective Action Plan:

PNCC agrees with this finding. The Chief Financial Officer will ensure regular monthly reconciliation of long-distance revenues will be carried out. Efforts will continue to procure and implement a system capable of generating data needed to support accounting of deferred/unearned airtime minutes.

This is a finding is a repeat and unresolved.

PALAU NATIONAL COMMUNICATIONS CORPORATION
(A Component Unit of the Republic of Palau)

Independent Auditor's Report on Compliance with Aspects of Contractual Agreements and Regulatory Requirements for Telecommunications Borrowers

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Year Ended December 31, 2020

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH ASPECTS OF CONTRACTUAL AGREEMENTS AND REGULATORY REQUIREMENTS FOR TELECOMMUNICATIONS BORROWERS

To the Board of Directors
Palau National Communications Corporation:

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Palau National Communications Corporation (PNCC), a component unit of the Republic of Palau, which comprise the statement of net position as of December 31, 2020, and the related statement of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated July 30, 2021. In accordance with *Government Auditing Standards*, we have also issued our report dated July 30, 2021, on our consideration of PNCC's internal control over financial reporting on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. No reports other than the reports referred above and our separate letter regarding recommendations concerning certain matters related to internal control, also dated July 30, 2021 related to our audit, have been furnished to management.

In connection with our audit, nothing came to our attention that caused us to believe that PNCC failed to comply with the terms, covenants, provisions, or conditions of their loan, grant, and security instruments as set forth in 7 CFR Part 1773, *Policy on Audits of Rural Utilities Service Borrowers*, Section 1773.33 and clarified in the RUS policy memorandum dated February 7, 2014, insofar as they relate to accounting matters as enumerated below. However, our audit was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding PNCC's noncompliance with above-referenced terms, covenants, provisions, or conditions of the contractual agreements and regulatory requirements, insofar as they relate to accounting matters. In connection with our audit, as except of the comments noted below, we noted no matters regarding PNCC's accounting and records to indicate that PNCC did not:

- Maintain adequate and effective accounting procedures;
- Utilize adequate and fair methods for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts;
- Reconcile continuing property records to the controlling general ledger plant accounts;
- Clear construction accounts and accrue depreciation on completed construction;
- Record and properly price the retirement of plant;

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- Seek approval of the sale, lease or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap;
- Maintain adequate control over materials and supplies.
- Prepare accurate and timely Financial and Operating Reports;
- Obtain written RUS approval to enter into any contract for the management, operation, or maintenance of the borrower's system in the contract that covers all or substantially all of the telecommunication system;
- Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in accordance with generally accepted accounting principles;
- Record depreciation in accordance with RUS requirements addressed in 7 CFR Part 1733.33(g); and
- Comply with the requirements for the detailed schedule of deferred debits and deferred credits; and
- Comply with the requirements for the detailed schedule of investments.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. At December 31, 2020, PNCC had no investments in subsidiary and affiliated companies that needed to be accounted for on either the cost or equity basis in accordance with the requirement of 7 CFR Part 1733.33(i).

* * * * * * * * *

This report is intended solely for the information and use of the management of PNCC, the Board of Directors and the Rural Utilities Service and supplemental lenders and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Burger Comer Magliari

BURGER COMER MAGLIARI
Koror, Republic of Palau
July 30, 2021

Unresolved Prior Year Comments
Year Ended December 31, 2020

STATUS OF PRIOR YEAR FINDINGS RESULTS

The status of unresolved prior year findings are disclosed within the Schedule of Findings and Responses section of this report on pages 57 through 60.